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SUBJECT: NIGERIA: ENERGY UPDATE, FEB 28

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¶1. This periodic update covering energy issues includes:
--Long Lines - Short on Answers; Fuel Crisis Continues
--Obasanjo Offers Onshore/Offshore Compromise
--Exxon-Mobil Produces Early from Yoho Fields, and
--Marginal Oil Fields Awarded

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LONG LINES - SHORT ON ANSWERS; FUEL CRISIS CONTINUES
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¶2. Just as the strike by workers of the Department of Petroleum Resources (DPR) was drawing to a close, Nigeria faced a new challenge in its energy sector; failed deliveries of finished petroleum caused serious fuel shortages throughout Nigeria last week, closing gas stations and forcing consumers to queue in lines not seen in years. In cities across Nigeria, lines snaked up to two miles from filling stations open only a few hours a day, and in some instances cars were simply left idle in place, adding to already chaotic traffic situations. Those consumers who were able to top off their tanks faced hiked prices by pump attendants or roadside black marketers, and those who used public transport paid higher fares when they managed to find their way onto a running vehicle. Area boys took advantage of the captive audiences, extorting money from motorists and passersby by intimidation and force.

¶3. Original theories that the DPR strike was the root of the gas lines gave way to the reality that Nigeria was simply running out of fuel. Nigeria imports nearly half of the refined petroleum products it consumes, and the Nigerian National Petroleum Corporation (NNPC) revealed that, in the wake of rising world petroleum prices caused by the growing tension over Iraq and the ongoing troubles in Venezuela, its suppliers redirected January and February shipments to more lucrative sales to the US and Venezuela. NNPC received just 30 percent of its contracted cargo in January, driving its fuel stock down from a 20-day reserve to an 11-day reserve by February 24. It is reported that NNPC has changed its import pricing formula to better reflect market trends, which will add a 10 to 20 percent premium to Nigeria's import costs.

¶4. To combat the shortages, NNPC ordered its second and third quarter shipments for delivery at the same time. The government also hopes to have its two refineries at Port Harcourt, which have been offline due to power problems and maintenance, running again soon. In the short term, two ships recently off-loaded 56 million liters of gasoline, but this may offer only a very brief reprieve as the daily national demand runs from 18 to 25 million liters. Further, an Exxon-Mobil official told Econoff that the sorry state of tanker facilities in Lagos will slow all off-loading, so that even when ships come in, fuel will not flow quickly to consumers. The situation did improve over the weekend, as gas lines receded and filling stations were returning to normal business hours this week. However, spot reports of new queues are coming in again as the week goes on.

¶5. Comment: The irony that the world's seventh largest crude oil exporter must import half of its refined petroleum products has not been lost on commentators and consumers alike. A fuel crisis reminding Nigerians of bygone days of military rule and of the fragile state of their economy comes at a terrible time for President Obasanjo, less than two months before the national election. With each new incident of ethnic violence, tensions are certain to rise if an ongoing fuel shortages continue to hamper the daily routine of business and personal lives. Suggesting the gravity of the government's concern over the situation, Information Minister Jerry Gana publicly blamed the gas lines on a smear campaign by Obasanjo opponents, and radio news reports quoted Obasanjo as saying there is no fuel shortage, but rather, people are simply hoarding gasoline. Fuel shortages will continue should

Nigeria fail to make market-competitive purchase offers for gasoline as US demand for it rises on the eve of possible conflict in Iraq and the upcoming summer driving season.

¶6. Comment continued: One positive outcome of this fuel shortage may be renewed interest in deregulating and commercializing Nigeria's downstream petroleum sector. John Pototsky, Managing Director of Mobil Oil Nigeria (MON), was recently quoted as saying that while MON enjoyed higher sales volume in 2002, its profits were very low due to the GON's pricing scheme. As recently as 2000 and 2001, downstream marketers imported gasoline since the world market price and the domestic retail pump price were aligned closely enough for the companies to manage small but notable profits. More recently, world market prices have far exceeded those that the retailers are allowed to charge at the pump, so the NNPC has essentially become the sole importer of gasoline. The downstream international operators import gasoline for the NNPC at world market prices, fuel that the NNPC sells at artificially low prices. Obasanjo's energy adviser, Rilwanu Lukman, was quoted as saying the system cannot be maintained at current prices owing to the large government subsidies it entails. A "BusinessDay" editorial called for a shift to free market mechanisms, including invitations to foreign companies to purchase and maintain existing refineries, pipelines and depots. End comment.

OBASANJO OFFERS ONSHORE/OFFSHORE COMPROMISE

¶7. President Obasanjo offered a compromise in the ongoing legislative battle over the allocation of oil revenue between the federal government and those states from which oil is extracted (reftel). In a letter read to the Senate this week, Obasanjo calls for abandoning the earlier proposals by him and the National Assembly for demarcating what production is onshore versus offshore for revenue sharing purposes. Obasanjo had previously proposed that a 24-mile contiguous zone off the coastline should be used to determine which production sites are subject to the special derivation fund, from which oil producing states are entitled to a 13 percent share of oil tax and royalties. The National Assembly's formula would have extended the reach of the derivation fund to the Continental shelf and the Economic Zone. Obasanjo now argues both plans have technical and political drawbacks, and instead, proposes that all production lying within 200 meters of water should be subject to the derivation fund.

¶8. An Exxon-Mobil representative confirmed that all existing producing oil fields lie within a 200-meter depth zone, which is roughly equivalent to the edge of the Continental Shelf. This proposal would then place all deepwater oil discoveries not yet producing outside the scope of the derivation fund and within the sole purview of the federated account, the funds of which are distributed on the basis of a complicated formula amongst the federal government and all states and local governments.

¶9. Comment: The Exxon-Mobil representative noted that prior to last year's Supreme Court ruling defining onshore and offshore to the federal government's advantage, Akwa Ibom state received three billion Naira each month from the derivation fund, but was left with no revenue from that account as a result of the ruling. (The federal government has been providing the state 600 million Naira per month in the intervening period, according to our industry source.) He estimates that Obasanjo's proposal will provide Akwa Ibom with the same revenue it previously enjoyed. Thus, he anticipates the littoral states will support Obasanjo's new proposal, as is evidenced by public support voiced by the governor of Delta State. If this measure is successful in the National Assembly, it could go a long way toward shoring up political support for Obasanjo in the South South; the leaders from the Northern states, however, are unlikely to easily accept any proposal conferring benefit to the South. End comment.

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EXXON-MOBIL PRODUCES OIL EARLY FROM YOHO FIELDS
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¶10. Exxon-Mobil has begun production from its Yoho development project two years ahead of schedule, by using a temporary floating, production, storage and off-loading (FPSO)vessel as an early production system (ESP). The Yoho project is a Mobil Producing Nigeria (MPN)and NNPC joint venture (JV), located in the relatively shallow waters of Oil Mining Lease(OML) 104.

The $1.2 billion project has estimated recoverable resources of 0.4 billion barrels of oil, and represents the first deployment of an ESP in West Africa. The Yoho JV will have a production capacity of approximately 650,000 barrels per day I(bpd), and while press reports indicate it is currently producing 90,000 bpd, an Exxon-Mobil executive told Econoff it is already reaching or exceeding 100,000 bpd.

MARGINAL OIL FIELDS AWARDED

¶11. After a sometimes contentious two-year process, the federal government this week announced 31 companies who have won licenses to operate 24 marginal oil fields in the Niger Delta. The fields may hold up to 2.3 million barrels of crude oil, and are considered marginal because each produces no more than approximately 5,000 bpd, which the major oil companies consider economically unviable for the scale of their operations. The GON hoped to spur development of indigenous companies, greater domestic income and more local jobs through the sale of these marginal fields. It reviewed bids from 66 companies, including several state-owned firms. Presidential energy adviser Lukman called on the winning firms to aggressively develop their operations, and implored the financial industry to assist these companies in raising capital.

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